BRIEF IN SUPPORT OF PETITION FOR CERTIORARI.

For the opinion below, jurisdiction, statutes involved, summary statement of matter involved, specifications of errors, questions presented, reasons for granting the writ, and prayer for writ, we respectfully refer the Honorable Court to the petition contained above.

Point I.

THE CIRCUIT COURT OF APPEALS ERRED IN CONCLUDING THAT MASSACHUSETTS LAW BARRED RECOVERY.

The majority is in accord with the dissenting justice that there are no Massachusetts cases squarely in point and that the Massachusetts law is not entirely clear. In such a situation the duty of a Federal court in seeking the "rule of decision" as required by Section 34 of the Federal Judiciary Act lies in either of two alternatives: It may examine relevant decisions and dicta of the Massachusetts courts and apply as the "rule of decision" that rule which in its opinion a Massachusetts court would have applied if the action was originally brought in the State court, or it may exercise its independent judgment and apply what it considers the most equitable principle as its "rule of decision." Which of these two alternatives it must take is a matter which should be decided by this Court, and which will be discussed in Point II of this Brief. It is the contention under Point I herein that, regardless of which alternative it should have taken, the Circuit Court decision, as it now stands, satisfies neither, and should be reversed on that basis.

A. Examination of the Ultra Vires Doctrine.

In order to ascertain the probable result if this cause had been brought in a Massachusetts State court, it is neces-

sary to critically examine the *ultra vires* doctrine as it has been applied generally and in the Massachusetts courts. In view of the fact that the Massachusetts courts have not of late passed upon this doctrine, recent trends supply an essential background in anticipating what future Massachusetts policy as to this doctrine will be.

The doctrine has been the subject of much adverse criticism in recent times. As the dissenting justice in the case at bar remarks: "This kind of defense is not so fashionable as it once was, and we ought not to be astute to extend it . . ." (R. 45).

See Fletcher, vol. 7, Ency. Corporations (1931), p. 619; 1940 Supp. p. 94.
Note, 16 Boston Univ. L. Rev. 194-199.
Carpenter, "Should the Doctrine of Ultra Vires be Discarded," 33 Yale L.J. 49.

Where recovery is sought against a corporation based on an *ultra vires* transaction, the doctrine has some meaning if the paramount policy is conceived to be the protection of the stockholders and creditors of the defending corporation. It may be that recovery based on activities beyond the scope of corporate powers should be limited to the amount of benefit received by the corporation. But to pervert this shield, as in the case at bar, so that it provides a defense to an action by a corporation to recover the value of benefits it has conferred upon others, is to discard all reason and to use the doctrine for a vindictive purpose, if there be purpose in it at all.

In recent years State legislatures, convinced of the injustice of the doctrine, and loath to await the evolvement of more salutary principles by the courts, have changed the effect of the doctrine by statute. In 1915 Vermont enacted the first statute of this type. In 1924 the Commissioner

on Uniform State Laws recommended a provision on this subject in the Ninth Draft of the Uniform Business Corporation Law. This provision became Sections 10 and 11 of the final draft of that law recommended in 1928.

See Handbook of the National Conference of Commissioners on Uniform State Laws (1928), pp. 334-335, 357-362.

The provisions of this Uniform Act have since been adopted in Louisiana, Idaho, Washington and Indiana.

See 4 U. of Cinn. L.R. 419, 434 (1930).
12 Wisc. L.R. 473 (1937).

More recently, statutes which go even further in abolishing the *ultra vires* doctrine have been adopted in California, Illinois, Michigan, Ohio, Minnesota, Pennsylvania and Wisconsin.

See 17 Calif. L.R. 529 (1929).
12 Wisc. L.R. 417 (1937).

B. The Doctrine of Ultra Vires as it has been Applied in Massachusetts.

The earliest cases in Massachusetts allowed a one-sided type of plea, allowing the corporation to plead *ultra vires,* but estopping the other party from so defending. This made for a rational and intelligible distinction.

See *Chester Glass Company* v. *Dewey,* 16 Mass. 94.
Old Colony Railroad v. *Evans,* 6 Gray, 25.
National Pemberton Bank v. *Porter,* 125 Mass. 333.

The *Old Colony* case, cited above, involved a suit by a corporation to specifically enforce an *ultra vires* contract for the sale of land. The defendant was estopped from pleading *ultra vires*, the Court stating at page 27:

> "A court of equity will enforce against a natural person his agreement to purchase of a corporation lands which it holds in violation of its charter, but will not enforce against a corporation its agreement to purchase lands for a purpose not authorized by its charter. The distinction is obvious: in the latter case to enforce the agreement against the corporation is to compel the application of its funds for a purpose not authorized by law; in the former case to compel the individual to take and pay for the property according to his agreement is the surest and most factual means of replacing in the treasury of the corporation, for its lawful use and the benefit of its stockholders, the funds which it had misapplied."

Davis v. *Old Colony Railroad*, 131 Mass. 258 (1881), involved a suit on an *ultra vires* guaranty against a corporation. The corporation was permitted to set up the defense. It is significant, however, that the corporation was the defendant and that no benefit was conferred upon the corporation in exchange for its assuming liability on the guaranty. Furthermore, the Court reviewed the older cases cited above and alluded to the distinction there made with favor at page 273.

In *Slater Woolen Co.* v. *Lamb*, 143 Mass. 420, 9 N.E. 823 (1887), a corporation was permitted to recover in an action of contract against a defendant who attempted to set up a plea of *ultra vires*. The Court stated at page 422:

> "If it be assumed in favor of the defendant that the contracts of sales in the case at bar were *ultra vires*

of the corporation, they were not contracts which were prohibited or contracts which were void as against public policy or good morals. The defect in them was that the corporation exceeded its powers in making them. The defendant under these contracts has received the goods and retained and used them. We think that the corporation can maintain an action of contract against the defendant to recover the value of the goods."

The next landmark in Massachusetts law is the famous case of *Nims* v. *Mt. Hermon Boys' School*, 160 Mass. 177 (1893), 35 N.E. 776. Justice Knowlton held a corporation liable in an action for a tort committed while the corporation was engaged in an *ultra vires* transaction, stating at page 179:

"Courts have frequently held that while such contracts, considered merely as contracts, are invalid, they involve no such element of moral or legal wrong as to forbid their enforcement if there has been such action under them as to work injustice if they are set aside. Courts have been astute to discover something in the nature of an equitable estoppel against one who, after entering into such a contract and inducing a change of condition by another party, attempts to avoid the contract by a plea of *ultra vires*. It is said that such a plea will not avail, that to allow it would work injustice and accomplish legal wrong. Many cases might be supposed in which it would be unjust to hold that one who had received the benefits of such a contract might retain them and leave the other party without remedy, as he might have in a supposable case where another had put himself at a disadvantage on the faith of the contract with him to commit a crime."

In *Nowell* v. *Equitable Trust Company*, 249 Mass. 585, 144 N.E. 749 (1924), a contract of guaranty was again involved and the Court permitted a corporation to set up the defense of *ultra vires* in a case where the corporation had not received any benefit for assuming the liability of the guaranty.

McLean Co. v. *Sidebottom*, 277 Mass. 158, 178 N.E. 284 (1931), is a case practically in point with the case at bar. It involved an action brought on a note received in an *ultra vires* transaction by a corporation. The case is prevented from becoming controlling authority due to the fact that the defense of *ultra vires* was not properly set up by the defendant in his answer. The language of the Court, however, makes it absolutely clear that, if the defense had been set up, it would have been rejected. At page 159 Mr. Chief Justice Rugg states:

> "If it be assumed that the defense of *ultra vires* was open the case at Bar comes within the principle stated by Mr. Justice Knowlton in *Nims* v. *Mt. Hermon Boys' School* . . . concerning contracts by a corporation outside its charter powers."

After quoting the portion from the *Nims* case, contained in our Brief, *supra*, the Court at page 159 stated:

> "That is a just and salutary principle. It would be contrary to every dictate of fair dealing and good conscience to permit a defendant to retain the proceeds of a loan inadvisably made to him by a corporation. At this stage of the case the distinction between a count for money lent and a count for money had and received by the plaintiff for the defendant's account is purely formal and ought not to be permitted to stand in the way of the accomplishment of manifest justice."

Perhaps the most adequate summary of Massachusetts law is contained in the illuminating dissent of Justice Magruder in the case at bar (R. 44). He states:

> "The opinion of the court cites four Massachusetts cases for the proposition that an *ultra vires* contract is void, no action thereon being maintainable. . . . (citing 4 Mass. cases). These are all cases of suits against the corporation on an *ultra vires* promise. It does not necessarily follow that *ultra vires* may be invoked as a defense when the corporation is suing the other party to a bilateral contract; the Massachusetts law on this is not entirely clear. . . . It is at least understandable to argue that if the *ultra vires* promise of the corporation is void, it is not good consideration to support a counterpromise by the other party. However that may be, the present is not a suit on a bilateral contract. It is a suit on the unilateral promise of the defendants contained in the note. Even though an *ultra vires* promise of the corporation may not be good consideration for a counterpromise, I do not see why the corporation's act of handing over the money should not be regarded as good and sufficient consideration to support the defendant's unilateral promise, and I find no decisions in Massachusetts holding the contrary on facts like the present. . . . This kind of defense is not so fashionable as it once was, and we ought not to be astute to extend it beyond the clear holding of the Massachusetts cases."

Point II.

THE CIRCUIT COURT'S CONFUSION IN SEEKING THE "RULE OF DECISION" AS REQUIRED BY SECTION 34 OF THE FEDERAL JUDICIARY ACT IN A CASE WHERE THERE ARE NO DECISIONS SQUARELY IN POINT BY ANY STATE COURT IN THE STATE INVOLVED PRESENTS AN IMPORTANT QUESTION OF FEDERAL LAW WHICH HAS NOT BEEN, BUT SHOULD BE, SETTLED BY THIS COURT.

A. The Split in the Opinions of the Justices was Due to the Lack of a Guiding Principle in the Application of Section 34 of the Judiciary Act in the Situation Presented by the Case at Bar.

Woodbury, J., states in the majority opinion: "While none of the Massachusetts cases above cited is squarely in point, we feel that the language used by the Court therein indicates that it would be held in Massachusetts that in the case at Bar no action could be maintained on the note." This reveals an attempt by the majority to predict the result if the action had been brought in a Massachusetts State court. Magruder, J., in his dissent states (R. 45): "Mindful of our duty under *Erie Railroad* v. *Tompkins*, 304 U.S. 64 (1938) I still think we are free to hold that under the Massachusetts law the defense of *ultra vires* is not available to the defendants in a suit against them on the note. This kind of defense is not so fashionable as it once was and we ought not to be astute to extend it beyond the clear holding of the Massachusetts cases." This suggests that it is Justice Magruder's position that when no case squarely in point exists, a Federal court is free to fashion an independent judgment.

B. The Result Reached by the Circuit Court in its Application of Section 34 is in Conflict with Decisions of Other Circuit Courts of Appeals on the Same Matter.

Thus the Seventh Circuit Court of Appeals, in *New York Life Insurance Company* v. *Jackson*, 98 F. (2d) 950, writ of *cert. den'd*, 305 U.S. 640 (1938), has held that, when the precise question presented has never been decided by a State court, the Circuit Court may exercise its independent judgment on such a question. Accord, *Hagan & Company* v. *The Washington Water Power Company* (C.C.A. 7th, 1938), 99 F. (2d) 614.

The Fourth Circuit Court of Appeals, in *Travelers Indemnity Company* v. *Plymouth Box & Panel Company*, 99 F. (2d) 218 (1938), has held that, where the complaining party has not referred the Circuit Court to any statutes or judicial decisions of the State contrary to the views entertained by the trial court, the decision will be affirmed on appeal.

The Eighth Circuit Court of Appeals apparently follows the independent judgment view where no cases in point exist.

Cass Bank & Trust Company v. *Sheehan*, 97 F. (2d) 935 (1938).

A District Court case appears to be in accord with the view of the majority in the principle case, holding that, where State court decisions are conflicting or vague, or where there are no State court decisions, the Federal court may decide the matter on the basis of what it believes the State court will ultimately and authoritatively declare.

Sampson v. *Welch* (D.C. Calif., 1938), 23 Fed. Supp. 271.

C. Regardless of Which View This Court should Adopt as to the Proper Application of Section 34 of the Judiciary Act, a Reversal of the Circuit Court Opinion will be Required.

If this Court should decide, in accordance with the majority of the Circuit Court, that the duty of a Federal court where State decisions are conflicting, vague or non-existent is to decide the matter on the basis of what it believes the State court will ultimately and authoritatively declare, a reversal will be required, since, as has been set forth in Point I of this Brief, the Circuit Court was in error in its conclusion as to what a Massachusetts court would have done.

If the independent judgment position is adopted, a reversal is similarly required. It might be urged that the majority opinion in the Circuit Court represents the independent judgment of the Circuit Court justices involved. If this were so, petitioner concedes that a reversal would not then be required. It is obvious, however, that the majority did not intend to exercise its independent judgment. The language of the opinion clearly reveals the mental process engaged in by the majority in reaching its result. It is stated (R. 43): "While none of the Massachusetts cases above cited is squarely in point, we feel that the language used by the Court therein *indicates that it would be held in Massachusetts* that in the case at Bar no action could be maintained on the note." (Italics supplied.)

It follows, therefore, that if the duty of a Federal court in such a situation is to apply its independent judgment, the majority of the court in the case at bar have not done so,

and that the only way to ascertain the independent judgment of said court, is to reverse and remand the case at bar.

Respectfully submitted,

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